IN THE UNITED STATES BANKRUPTCY COURT
FOR THE NORTHERN DISTRICT OF TEXAS
FORT WORTH DIVISION

IN RE:	§	
	§	
EXPRESS ONE INTERNATIONAL, INC.,	§	
Debtor.	§	CASE NO. 02-41981-DML-11
	§	

MEMORANDUM OPINION

Before the Court is Debtor's Motion seeking authority to use cash collateral (the "Motion"). The Motion is supported by Bank of Nova Scotia ("BNS"), Administrative Agent under Debtor's prepetition Credit Agreement, and by the Official Committee of Unsecured Creditors (the "Committee"). The Motion is opposed by Texas Capital Bank, N.A. ("TCB"), assignee of approximately 14% of amounts loaned to Debtor under the Credit Agreement[1] (BNS and TCB are collectively referred to as "Lenders"), and by a group of several creditors (the "Aircorp Creditors") that assert claims against Debtor arising from certain leases. The Aircorp Creditors are affiliated with former owner - officers of the Debtor who are involved in litigation with the Debtor in state court.

Disposition of the Motion is within the Court's core jurisdiction pursuant to 28 U.S.C. §§ 1334 and 157 (b)(2)(M). The Court held a hearing on the Motion on April 5, 2002. Antecedent to addressing the Motion, the Court is faced with the following issues: whether TCB has a right independent of BNS acting in its capacity as Administrative Agent to contest whether Debtor is

[1]The balance of the loan to Debtor was made by BNS.

providing adequate protection to Lenders[2]; whether the proposed cash collateral order would constitute a sub-rosa plan in violation of *In Braniff Airways, Inc.*, 700 F.2d 935 (5th Cir. 1983) (*see also In re First South Savings Ass'n*, 820 F.2d 700, 714 (5th Cir. 1987)); and whether the Credit Agreement[3] is not applicable in the case and so does not define the relationship among Debtor, BSN and TCB because it falls within 11 U.S.C. §365(c)(2). Seeking guidance on these questions, the Court asked that the parties submit briefs on these and any other subjects they might deem germain by April 10. Despite the short time allowed them, the parties have provided the Court with excellent memoranda in support of their respective positions. These have been of considerable assistance to the Court in deciding this matter. This Memorandum Opinion constitutes the Court's findings of fact and conclusions of law. *See* FED. R. BANKR. P. 7052 and 9014.

I. BACKGROUND

Debtor was engaged in the air freight business. Its principal customer was Emery Worldwide Airlines, Inc. ("Emery"). Emery carried mail for the U.S. Postal Service and subcontracted with Debtor. This subcontract in recent years accounted for more than half Debtor's business.

In August, 2001, the Postal Service terminated its contract with Emery. This in turn led to the end of Debtor's subcontract. Though Debtor asserts, through Emery, entitlement to a substantial claim as a result of the termination of the arrangement with the Postal Service, loss of the subcontract, the downturn in the economy and competition for business have caused Debtor's air

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[2]Debtor contested the standing of TCB to be heard at all. The Court, however, ruled during the hearing that TCB was at least a party in interest within the meaning of 11 U.S.C. § 1109. As such TCB would be entitled to be heard at a minimum in any contested matter in which it had an economic interest. *See Fuel Oil Supply and Terminaling v. Gulf Oil Corp.*, 762 F. 2d 1283 (5th Cir. 1985). The Motion is a contested matter (*see* FED. R. BANKR. P. 4001(b)(1)) in which TCB clearly has an economic interest.

[3]The same issue might be posed regarding the Forebearance Agreement (as hereinafter defined).

freight business to become virtually moribund. Between the filing of this chapter 11 case on March 14, 2002, and the April 5 hearing, Debtor flew only one, three segment revenue flight.[4]

Prior to the filing, Debtor and BNS, with the participation at first of TCB, negotiated a document, the "Forbearance Agreement," which addressed the relationship between Debtor and Lenders in light of Debtor's deteriorating situation. The Forbearance Agreement was executed by BNS (purportedly as Administrative Agent for Lenders) and Debtor. Pursuant to the Forbearance Agreement, Debtor wire transferred $4,000,000 to BNS for the benefit of Lenders, reaffirmed, granted or agreed not to contest Lenders' liens on certain causes of action (including the claim against the Postal Service), agreed on terms for use of cash collateral in any ensuing chapter 11 case, and provided for Debtor's continued operations while liquidating certain assets. Under the Forbearance Agreement, BNS, as Administrative Agent, also agreed to certain benefits for Debtor's unsecured creditors subject to their acknowledgment of the validity of Lenders' liens, to the release of Debtor's principals, and to certain payments to insiders. The parties undertook to agree on a plan of reorganization and for disposition of other matters. Immediately after execution of the Forbearance Agreement, Debtor filed this case.

In the Motion, the Debtor proposed initially to incorporate the Forbearance Agreement in a final cash collateral order. Debtor and BNS have since retreated from this position. BNS, in its brief, states that it will consent to use of cash collateral provided only that the budgetary terms of the Forbearance Agreement are adopted in the order. The Court understands BNS to refer to paragraphs 9 and 10 of the Forbearance Agreement and the appended budget. At the April 5 hearing Debtor

[4]The Debtor also repositioned at least one aircraft–a "non-revenue" flight. Non-revenue flights may be at a cost to the Debtor.

indicated its concern was obtaining use of cash collateral, whether or not that included approval of the Forbearance Agreement.

II. PRELIMINARY MATTERS

A. Sub Rosa Plan:

Because of Debtor's and BNS's change in position, the Court need not rule on whether incorporation of the Forbearance Agreement into a cash collateral order would constitute a sub rosa plan. Portions of the Forbearance Agreement (e.g., return to unsecured creditors) turn on contingencies, and it may be that the Court would have concluded that these contingencies and other features save the Forbearance Agreement from crossing the *Braniff* line. Though the issue is moot now, it may arise in a different context later in the case.[5]

B. Standing of TCB:

The Court has already ruled that TCB is a party interest. The question remains whether it has a right independent of BNS to seek adequate protection. Both BNS and Debtor vigorously assert BNS's authority under the Credit Agreement as Administrative Agent to agree to terms for the use of cash collateral pursuant to 11 U.S.C. § 363(c)(2). They contend that TCB cannot contest BNS's determination as to what constitutes adequate protection. In this argument, besides the Credit Agreement, BNS and Debtor rely on the Security Agreement[6] by which Debtor granted the liens which entitle the Lenders to the protection of § 363(c)(2).

TCB, for its part, points to notes it holds directly from Debtor. Though TCB did not develop

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[5]The Court does not at this time make any finding or ruling concerning Debtor's ability to assume the Forbearance Agreement under 11 U.S.C. § 365.

[6]The Security Agreement was not introduced into evidence on April 5. However, BNS appended a copy to its brief.

this argument fully, the Court concludes that as payee of a note, TCB is unquestionably the holder of a claim within the meaning of 11 U.S.C. §101(5). The claim of TCB is secured to as great an extent as is BNS's, and, as such, entitles TCB to the benefits of 11 U.S.C. §363(e). *See In re Sweetwater*, 40 B.R. 733 (Bankr. D. Utah 1984), *aff'd*, 57 B.R. 743 (D. Utah 1985).

Moreover, the Court's reading of the Security Agreement supports its view that TCB has an independent right to adequate protection. Section 2.1 of the Security Agreement states that Debtor "hereby pledges to the Administrative Agent for its benefit and the ratable benefit of each of the Lender Parties, and hereby grants to the Administrative Agent for its benefit and the ratable benefit of each of the Lender Parties a security interest. . .in the collateral."

From this language the Court concludes that TCB was granted a beneficial interest in the Lenders' collateral. The drafters of the Bankruptcy Code consistently intended references to interests in property to be read broadly. *See, e.g.*, 11 U.S.C. § 363; 3 COLLIER ON BANKRUPTCY ¶ 363.03[3] (15th ed.. rev. 2002); S. REP. NO. 95-989, 95th Cong. 2d Sess.(1978). See, similarly, the breadth of property interests covered by 11 U.S.C. § 541(a); *See* 5 COLLIER ON BANKRUPTCY ¶541.04 (15th ed. rev. 2002). Since, TCB had an "interest" in the underlying collateral it also had an interest within the meaning of 11 U.S.C. § 363(a) in cash collateral. Under §§ 363(c)(2) and 363(e), it is clear that TCB is entitled to adequate protection. Whatever the Credit Agreement may provide, it cannot supercede the specific terms of the Bankruptcy Code.[7] *See Ginsberg v. Lindel*, 107 F.2d 721, 725-26 (8th Cir. 1939).

C. **Section 365(a)(2)**

[7]Whatever effect TCB's decision to act on its own behalf may have had on its realtionship with BNS (or the Debtor) under the Credit Agreement is beyond the scope of this Memorandum Opinion.

In light of elimination of the sub-rosa plan issue and the Court's disposition of any question of TCB's right to demand adequate protection, § 365(c)(2) no longer is relevant to the Court's decision. The Court will move on to the basic issues raised by the Motion: whether Debtor should be authorized to use cash collateral and whether it can adequately protect Lenders.

III. DISCUSSION

A. Conflicting Interests of the Parties

Though all of the parties have been most helpful to the Court in eliciting evidence and providing guidance on the law, the point has been made in some briefs that several of the parties potentially have agendas at odds with the Debtor's rehabilitation. In reaching its decision, this Court will keep in mind the potential non-bankruptcy interests of the parties. The position of the Aircorp Creditors may be influenced by their involvement in litigation with the Debtor. Similarly, three of four members of the Committee are allegedly investors, possibly insiders and the holders of subordinated debt.[8] Only one member of the Committee is a trade creditor. TCB, which holds but a small portion of the debt incurred by Debtor under the Credit Agreement, as other parties suggest, may be seeking leverage to force BNS to buy out its position.

The Court is not prepared to impute improper motives to any party. The positions taken by each party were appropriate under the law and suitable for this Court's consideration. However, the Court must be careful to fashion relief that accords with the Bankruptcy Code and with the interests of Debtor's estate and creditors. It is a fact of life that some chapter 11 cases represent but one aspect of a broader strategic situation. If this is such a case, it does not automatically follow that the

[8]Under the Forbearance Agreement special provision was made for subordinated noteholders to receive return on their investments, notwithstanding their purported subordination to the debt owed Lenders.

parties are acting in bad faith.[9] The Court will take into account the multiple interests various of the parties may have only by approaching critical issues such as that presented by the Motion with extra caution.

B. Analysis

The question before the Court is whether or not to authorize Debtor to use cash collateral. The Court's decision must turn on (1) whether TCB,[10] is "adequately protected" and (2), with appropriate deference to Debtor's business judgment, whether the proposed use of cash is consistent with the interests of creditors and the estate.

The Lenders are entitled to adequate protection only to the extent that use of cash collateral will result in deterioration of their secured claim. *See United Sav. Ass'n v. Timbers of Inwood Forest, Ltd.*, 484 U.S. 365, 108 S. Ct. 62, 98 L. Ed.2d 740 (1988). Were the Lenders overcollateralized, the question of adequate protection would not arise. Such evidence as the Court has, however, suggests Lenders are under-collateralized. They are thus entitled to adequate protection to the extent that use of cash collateral will result in reduced recovery on their secured claims.

TCB misperceives, however, what this means. In the first place, entitlement to adequate protection does not require that a lender have an iron-clad guaranty against loss. 11 U.S.C. §507(b) provides for cases where protection of an interest proves inadequate. If the Court were expected to provide to a secured creditor absolute certainty that its position would not deteriorate, there would

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[9]Though the Court will act appropriately if it concludes any party *is* acting in bad faith.

[10]Since BNS has agreed to terms for the use of cash collateral, the question is only whether those terms will adequately protect TCB.

be no reason for § 507(b). *See In re Becker*, 51 B.R. 975, 979 (Bankr. D. Minn. 1985); *In re California Devices, Inc.*, 126 B.R. 82, 85 (Bankr. N.D. Calif. 1991).

TCB places much emphasis on 11 U.S.C. §361(3), which, it argues, equates "adequate protection" with "the indubitable equivalent" of the interest for which protection is given. This language, TCB suggests, requires an absolute assurance against loss, which the Debtor does not provide. But the thrust of §361(3) is not only weakened by the need Congress found to clarify that an administrative expense claim under 11 U.S.C. §503(b) does not amount to indubitable equivalency. It is belied by the Fifth Circuit's refusal to find in the term as used in 11 U.S.C. §1129(b)(2)(A)(iii) a promise of an improved or even equal collateral position. *See Sun Country Dev., Inc.*, 764 F.2d 406 (5th Cir. 1985). While the context of protecting an interest in property under §363 is not the same as under §1129, *Sun Country* sheds considerable light on what is required as the "indubitable equivalent" of an interest in property.

Moreover, the Court must take into account what is being protected. If a creditor holds a lien which is subject to legitimate attack, the possibility of the lien's avoidance may be considered in balancing the creditor's right to protection against the debtor's need to use the collateral. In the instant case, the Postal Service claim is expected to produce some cash Debtor proposes to use. As discussed, *infra*, that lien may be subject to challenge.

The Debtor wishes to use cash collateral to fund (1) a liquidation effort, (2) litigation and (3) ad hoc flight operations. Except for the liquidation of assets, the Debtor's needs will clearly lead at least at first to a deterioration in its cash position. Since all its cash is arguably subject to the liens of Lenders, and since no dispute has yet surfaced regarding the validity of Lenders' liens on Debtor's cash collateral, TCB (as well as BNS) is entitled to receive adequate protection for cash used.

Debtor offers (1) replacement liens on the receivables it proposes to generate through flight operations, (2) a lien on the Postal Service claim, and (3) a lien on other litigation.

TCB argues this is not enough. TCB claims Lenders already have a lien on the Postal Service claim. It and the Aircorp Creditors mock the Debtor's suggestion that it can generate receivables to offset the losses the Lenders will suffer, asserting Debtor cannot possibly operate profitably. Finally, TCB argues that a lien on the other litigation is inadequate to satisfy the requirements of adequate protection – even if that litigation is not subject to the existing Security Agreement.

The Court considers the terms of the Forbearance Agreement evidence that BNS is not so confident of the lien on the Postal Service claim, even assuming there is other documentation perfecting the lien granted by the Security Agreement.[11] Nor does the Court consider the Security Agreement undoubtedly sufficient to grant such a lien on the Postal Service claim or any other litigation. However speculative the other litigation may be, the Court finds that the Postal Service claim, at least, has significant value. Just as the Court might consider a weakness in a lender's lien on cash collateral in determining necessary adequate protection, the Court holds that shoring up the Lenders' lien on disputed but valuable claims can constitute protection under 11 U.S.C. 363(e).

The Court is also not prepared to write off the chance that Debtor can offset losses to the Lenders through operations. The Aircorp Creditors suggest Debtor does not even have access to aircraft. Yet even it if cannot lease planes,[12] Debtor owns four aircraft. While it has tendered these

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[11]The record, however, is insufficient to prove the perfection of any lien by any party.

[12]Debtor's CEO, Kevin Good, ("Good"), testified Debtor expected to lease a plane from Prewitt Leasing. Prewitt Leasing was present at the time hearing and appeared through counsel. It did not contradict Good's testimony. Debtor has leased one of Prewitt Leasing's aircraft since the commencement of the case, and the Court infers that a similar arrangement may be made in the future.

to Emery in connection with the Postal Service claim, no evidence was introduced to show they were unavailable for Debtor's use.

Good testified that Debtor receives numerous inquires about its availability for hauling cargo. Good is better placed than Robert Gallo, an expert witness called by TCB, to assess Debtor's relations with potential customers and Debtor's ability to contract with them. This is particularly true of the "ad hoc" business on which Debtor expects principally to rely. The Court finds that the preponderance of the evidence shows that Debtor will be able to generate business and obtain access to aircraft. While the Court may be skeptical as to the potential for Debtor's profit, BNS's willingness to accept Debtor's projections[13] together with the testimony of Good and Dale Pound, Debtor's CFO, is sufficient to convince the Court that there is a reasonable possibility that Debtor can at least offset costs through continued operations.

Good also testified that the proposed budget was a "worst case" scenario. During the hearing items in the budget were identified that are not necessarily going to be paid, including retention and success bonuses, consulting fees and other professional fees. Even if operations of Debtor failed to meet Good's expectations, these items could prove sufficient to eliminate the loss of $991,000 projected by the Debtor.

Moreover, as Good testified, employees necessary to liquidation of assets and pursuit of litigation are also involved in operations. As their retention would be appropriate in any case, part of the cost attributable to ad hoc operations would be incurred anyway. Since other costs of

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[13]The Court considers BNS's position particularly significant. With much more at risk than TCB, BNS, which also has more experience with Debtor and its management, was not only willing to accept Debtor's projections. It was prepared to make substantial concessions in the Forbearance Agreement in exchange for Debtor's performance.

operations will vary depending on how much business Debtor does, the risk to TCB from authorizing use of cash collateral for operations is minimal.[14] Certainly at this early stage of the case the Court is reluctant to end Debtor's aspirations to save its business. As continued operations may aid in preserving Debtor's FAA Flight Certificate and in pursuit of the Postal Service claim (both valuable assets), the Court finds that it is in fact in TCB's interest to allow use of cash collateral to fund operations.[15]

IV. RELIEF TO BE GRANTED

The Court is not without doubt in this case. It is persuaded only by the barest preponderance of the evidence that the replacement lien on receivables and the litigation and Postal Service claim liens satisfy the requirements of 11 U.S.C. §§ 363(c)(2)(B) and 363(e). The Court is also not overly optimistic about Debtor's operating prospects. Nevertheless, for Debtor to have any hope of success, it must be ensured at least five weeks of use of cash collateral. Accordingly, the term of the order entered pursuant to this opinion shall extend through the term of the budget proposed by the Debtor (Debtor's Exhibit 3 at the April 5 hearing) and, absent substantial variation from Debtor's projections, shall not be subject to reconsideration before May 17, 2002.

As adequate protection to Lenders, liens shall be granted as proposed in the Motion. Because TCB has raised concerns, as additional protection for it, the order authorizing use of cash collateral shall provide that any claim of TCB under 11 U.S.C. § 507(b) shall be senior to any claim asserted

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[14]Where a Debtor's survival is at stake, it is not inappropriate to put a lender at some added risk. *See In re Prime, Inc.*, 15 B.R. 216, 220 (Bankr. W.D. Mo. 1981). Here the Court finds that this approach would be in order even if TCB were not, as the Court concludes, in fact adequately protected.

[15]Debtor is committed to shutting down its in-flight operations should its losses reach $1,000,000. As TCB, with 14% of the loan, thus faces little more than $140,000 in exposure, it clearly has a greater likelihood of improving its position than of suffering serious loss.

by BNS under that section. The order also will provide that salaries in excess of $8,500 per month shall be paid in arrears and, should authority to use cash collateral be revoked, shall, to the extent at that time unpaid, be satisfied by a cost of administration claim. Furthermore, the Debtor shall undertake a review of its personnel needs and provide to the Court by April 22 a justification for the continued employment of each employee. The Court questions why Debtor's 26 employees include a President, an in-house lawyer and a CEO (who is himself a lawyer). Should this case proceed to a successful end, the Court is prepared to ensure generosity to all employees. Until then, the employees, especially at the higher levels, must bear a share of the risk of failure.

BNS has agreed that the Forbearance Agreement need not be incorporated into the order granting use of cash collateral. The exception is budgetary terms. Besides the budget appended to the Forbearance Agreement (identical to Debtor's Exhibit 3), these appear to be limited to ¶¶ 9 and 10 of that document. The Court will adopt ¶¶ 9(a), 9(b) (subject to retention of the Court's authority to address any budget item in the future), 9(d), 9(f), and 10. Any report furnished by Debtor pursuant to any of these paragraphs shall be provided to TCB, the Committee and, upon his request, the United States Trustee. Nothing herein shall authorize the Debtor to pay any non-employee professional or take any action outside the ordinary course of its business--regardless of the terms of the budget or ¶¶9 and 10 of the Forbearance Agreement.

BNS, by separate correspondence, has asked that the Court eliminate from any cash collateral order its prior requirement that the collateral of Lenders remain subject to 11 U.S.C. § 506(c). The Court is prepared to limit § 506(c) charges to those proven to have actually preserved, benefitted or brought about realization upon Lenders' collateral. Beyond that the Court is unwilling to prohibit surcharges. As to BNS's request that any future trustee not have authority to question its liens,

subject to any applicable preclusive doctrine, the Court cannot in good conscience do more than limit to 30 days after his appointment the time within which any such trustee may assert such a challenge.

An order shall enter consistent with this opinion, which order shall be effective from April 12, 2002.

Signed this the 16 day of April, 2002.

HON. DENNIS MICHAEL LYNN
UNITED STATES BANKRUPTCY JUDGE